OVERVIEW

COVID-19: Contracts: Overview 18.05.20

COVID-19

This guidance is to allow ECA Members to give consideration to those contractual risks which would usually be overlooked, such as biological contamination, pandemics and/or natural catastrophes. This contractual guidance note covers the basic checklist of issues in the context of construction and

1. Summary

The following is a list of considerations in the event that you are unable or impaired from proceeding with/completing works under a construction or FM contract (whether one-off or a framework basis).

Note: If you don't have a contract in place (oral or written) yet, the offer will most like have been or will be cancelled/temporarily withdrawn until the outbreak is over.

If not, this may be because clients are trying to lock desperate tenders into pre-COVID rates and productivity levels under terms & conditions which do not cater for pandemics. You should question your traditional tendering system as it is based on pre COVID-19 productivity rates and amend it according to new productivity rates under current safety measures for construction and FM issued by industry and Government.

The following considerations are only for when a contract has come into existence – which in the majority of cases in our sector is through behaviour, rather than through 'wet-ink' signed documents.

This guidance does not cover your ability to reach non-contractual agreements through collaborative commercial dialogue which should always be considered alongside your contractual position.

ECA Members must take proactive:

a) steps to risk assess their business in the following key areas:
   - materials suppliers
   - labour availability or surplus
   - KPI/service credit performance measurement systems
   - Payment
   - Time management/call-out/emergency response systems
   - Disruption costs

b) decisions to mitigate that risk utilising:
   - a considered approach
   - documented decisions
   - following a strategy that minimises loss to your business

- which can be used to support your contractual position with other parties

2. Risk assessment

We suggest ECA businesses consider the impact of COVID19 in the following ways:

- **Insurance** – Ensure you act in line with your insurance policy requirements for business continuity, employer's liability, public liability, contractors' all risks and professional indemnity, so that you do not undermine your coverage and reserve your ability to make claims. You may wish to ask your insurers what their expectations are of you in regard to each type of cover and take particular note of time limits for notices or claims.

  Business interruption insurance policies in particular may cover disruption caused both by the disease itself and by public policy responses to it, such as enforced quarantines. However, there are often exclusions in such policies for example:

  - Severe Acute Respiratory Syndrome (SARS)
  - Anthrax
  - Any mutation (swine flu) or H5N1 (bird flu) that manifest itself as a human infectious or human contagious disease
  - Any infectious diseases which have been declared as a pandemic by the World Health Organisation (COVID-19)

  Insurers only tend to cover these circumstances where Government issues edicts (not just guidance) forcing society to conform to disruptive rules.

  The policy coverage may only compensate for damage suffered, rather than simply disruption caused by the virus. This is an important but subtle difference in the policy cover.

  You should also be aware of; the notification requirements so that you do not undermine your ability to claim, and the caps on the policy cover - it is rare for any insurance policies to be unlimited.

- **Clients –** ask clients to inform you of their contingency/new COVID-10 safe arrangements so that you can reassure them of your business continuity and be perceived as proactively managing the situation.

- **Funders and banks –** if your finance function can model various scenarios to your cash-flow, that may inform you on whether you need to secure additional credit. While the interest rate may be low, the industry is seen as low margin and high risk for insolvency, which in the event of global recession can lead to vastly reduced lending capacity to the SME construction market.

- **HMRC** – HMRC have set up a specific COVID-19 helpline on 0800 0159 559 to discuss arrangements for delaying and deferral of payment of taxes www.gov.uk/difficulties-paying-hmrc. If you are upfront and proactive – you must reach out to HMRC before you are overdue - HMRC will most likely discuss a Time to Pay Arrangement with HMRC is a debt repayment plan for your outstanding taxes. Companies that have defaulted on their payments to settle their Corporation Tax, VAT and/or PAYE can ask HMRC for extra time to pay. They will usually agree that you can pay it back over 6-12 months.

- **Communications -** Setting up project specific communication networks with your supply chains.

- **Safety -** Reviewing safety critical elements of your projects will help manage and mitigate the risk and determine new norms in terms of productivity rates – this will allow you to better determine your true tendering rates within a COVID-19 environment in line with industry and Government guidance.
- **Programming -** Review programmes to factor in disruption and productivity impacts from COVID19.

Other issues are addressed in our guidance notes on business continuity, site safety, health & safety legal requirements and support via Government announcements.

3. Who holds the risk?

In the construction supply chain, there is one constant which remains unchanged whenever a pandemic strikes - the legal risk-holder for any resultant business disruption. With international and/or national restrictions being placed on people and goods/materials contractors will need to be aware of the impact this may have on the ability to deliver their contracts.

4. Change in law

This might form the basis of your contractual rights to make a claim rather than relying on less specific rights like force majeure or frustration which may be harder to prove (and therefore most costly), but be careful as there is an inherent difference between Government guidance (non-binding) and law (which is binding) – the latter usually invokes a change of law clause.

- Do you have a clause which specifies what happens if a change in law or a Governmental direction (local or central) takes place?
- What are the implications for the parties regarding time for completion? claims for loss, variations for price etc.?

5. Notices

Factors to consider with reference to contractual communications and their legitimacy are:

- What are your notice provisions?
- How are notices validly served?
- Are the communications you are receiving contractually valid under notice provisions and in accordance with the contract? – don't accept WhatsApp or Messenger as valid communications in the heat of the moment!
- When are they deemed to arrive/received?
- Should you give early warning, programming, warning notices?
- How often do you have to update these notices under the contract (even if there is no change in the information)?
- Do any notices need to be given under other arrangements – e.g. collateral warranties, bonds, guarantees etc.?
- Just because someone has been furloughed doesn't means the communication/notice is not valid. It will be in the vast majority of cases because the contracts are usually Business2Business and specify a generic or nominated postal and email address for these purposes.

6. Time & Money

A starting place is to ask yourself, what are your programming/time obligations under the contract and how do you operate them?

You may be obliged to notify your client of delays to completion, milestones and/or sectional completion. For example, JCT sub-contracts require the sub-contractor to notify forthwith (JCT DBSub/C 2016 c.2.17.1) of any delays and/or loss and expense (c.4.15.1 of JCT DBSu/C 2016, specifies '*as soon as reasonably practicable*' for loss & expense), whilst the NEC3 Sub requires the sub-contractor to give 'early warning' notices (NEC3 Sub c.16.1) which have the effect of preserving the sub-contractor's right to make claims later on for 'compensation events' (under c.60.1 NEC3 Sub). NEC3 Sub also requires the sub-contractor to make claims within an 7-week period (c.61.3 8 weeks under the main contract) before becoming time-barred from being able to do so.

Also remember to check any bespoke amendments to the industry standard forms which may change the processes, procedures and risks involved.

The following clauses of your contract may become relevant:

- **Instructions/Variations/Changes** – Where your client instructs you, you will want to formalise that instruction so that it is incorporated into the contractual machinery and gives you any rights to claim back any additional time and money you may be entitled to, so that you do not bear the risk of the disruption to your delivery caused by COVID19. Do not take oral communications as good enough under the contract! – JCT DBSub/C 2016: c.2.19.1 & .2 *variations and changes*, 2,19.5 *employer's instructions*, 2.19.1.3 *deferment of possession…*, c.2.19.8 & .9 *impediment or prevention…site not safe,* NEC3 Sub c,60.1(1).(4) & (5), *COVID-19 access restrictions… c.*60.1(2), *a Change ensues…* c.60.1(18, *flexible working arrangements engineer, architect, employer delay* c.60.1(3), (5), (18) and (19)).
- **Materials** – Where materials are free issued, the contractor should claim for a delay, impediment or prevention by the client or those for which it is responsible. Where you are responsible for supply of materials, you will want to ensure you are, in addition to contingency planning with your own suppliers, not responsible for delays due to circumstances beyond your reasonable control and that this includes where materials are simply unavailable. You may also have to consider alternative suppliers where the risk of delay or impediment sits with you. See NEC3 Sub c.60.1(3), (4), (16) and (18)
- **Change in law** – where the UK Government introduces specific legislation to deal with the current arrangements, your contract will dictate who takes the risk of changes in law (JCT DBSub/C 2016 c.2.19.15 *exercise of statutory power…*JCT DBSub/C 2016 or if NEC3 NEC OptionX2 additional condition is included).
- **Suspension –** Does either party under the contract have a right to unilaterally suspend the contract? – what if the site is shut? If so, what is the procedure? What are the circumstances? Does it lead to termination after a consecutive or cumulative period of suspension? What can you get paid for? (JCT DBSub/C 2016 c. 2.19.7 *suspension by contractor…* or where ordered by employer/engineer/architect due to virus NEC3 Sub c.60.1(4)).
- **Notice provisions –** What are the contractual procedures for sending contractual notices and what should be included? Make sure you do not fall foul of the contract, by simply not complying with the prescribed procedure. The contract will follow a prescribed process and stick to this rigidly supplying all possible record keeping in support of time and money claims. C.1.7 JCT DBSub/C 2016 and c.13.1 NEC3 Sub.

- **Time-bars & conditions precedent** – Ensure you comply with any pre-conditions for making claims or giving notices, so that you are not barred from doing so because you have not complied with a time constraint or pre-condition (JCT DBSub/C 2016 c.2.17.1/NEC3 Sub 7-weeks c.61.3 8). Therefore, better to give a notice and retract, than not to have given it at all.
- **Duties to mitigate –** If the contract states you must take all steps (reasonable or otherwise or using '*reasonable*' or '*best*' '*endeavours*') to mitigate the effect of delay and disruption or instructions, ensure you have done so and have kept meticulous records – c.2.18.6 JCT DBSub/C 2016.
- **Bespoke amendments –** Ensure that you have a complete record of the contract and are complying with additional terms and not just the standard form industry JCT or NEC style contract on which the actual contract is only loosely based.

7. Force Majeure

Force majeure is a contract right, i.e. it only exists if there is some kind of clause giving you the right to claim relief where you are precluded from carrying out your contractual obligations by some kind of 'act of god'.

The following is a checklist of issues to consider under a force majeure claim:

- Is there a clause?
- Does it cover epidemics/pandemics?
- What triggers it?
- What are the consequences for time, money (compensation/loss & expense/price), suspension and termination?
- What evidence is required?
- When was the contract entered into?
- Do you have parent or director guarantees and/or bonds in place which will still operate to cover your default in force majeure circumstances?

Affected parties should consider whether their contracts contain force majeure clauses and whether the outbreak falls within the protection offered by the relevant clause.

"Force majeure", from the French "superior force" (read: 'Act of God') describes circumstances outside of the control of either party in a contract which prevents work from proceeding.

In English law, "force majeure" has no recognised meaning. A clause stating that the "parties agreed that if performance is disrupted or prevented by force majeure, the parties right and remedies shall be as follows…" will almost certainly be held void for uncertainty unless the term is defined elsewhere within the document.

The protection afforded by the clause will depend on the precise drafting. In the event of a dispute as to the scope of the clause, the English courts will apply the usual principles of contractual interpretation.

An example clause is below:

> *Notwithstanding anything else contained in this Agreement neither party will be liable for any delay in performing its obligations herein, if such delay is caused by circumstances beyond its reasonable control (including without limitation any delay caused by an act or omission of the other party).*

In difficult cases, the client may try and argue the circumstances were not beyond the contractor's reasonable control as the consequences of COVID19 have been emerging over the past 8 weeks and allegedly could have been planned for. We would hope this argument would not be tolerated by a judge or adjudicator, but in spurious cases it might be used as a reason, in the interim, to delay payment.

The first death from unknown cause pneumonia was reported to the World Health Organisation in China on 31st December 2019. So, would a global response or shut down have been reasonably foreseeable after the media started reporting the incident around January 10th, 2020? Could the argument be put forward that you should have planned for the impact of the virus?

The words '*including without limitation…'* ensure that it is not just circumstances arising from an act or omission of the other party that allow the clause to be enacted.

> *Subject to the party so delaying promptly notifying the other party in writing of the reason for the delay and the likely duration of the delay, the performance of such party's obligations will be suspended during the period that the said circumstances persist, and such party will be granted an extension of the time period for performance of duties and obligations under this agreement equal to the period of the delay.*

Note: this gives you time but not money. What if the extension, i.e. the consequential effect on the contractor's ability to deliver the contract is greater than the '*period that the said circumstances persist*'? Under this clause you will only be able to claim an equivalent period.

> *Either party may, if such delay continues for more than 5 weeks terminate this Agreement on giving notice in writing to the other in which event neither party will be liable to the other by reason of such termination.*

Is 5 weeks an appropriate period? Whilst neither party will be liable, what can the contractor claim – works done to date (complete or not)? Loss of profit on the remaining works? Wasted expenditure to date? What is the process for wrapping up your account?

Are you relying on COVID19 or Governmental regulation/guidance following COVID19?

> Is there a test 'prevention', 'hindering', 'unable to deliver' – this will dictate the burden and nature of proof required in order to present a robust claim with the required level of substantiation (record keeping will be paramount to proving your claim).

8. Frustration/prevention

Under English law, if a contract becomes impossible to perform as a consequence of the COVID-19, it may be open for a party to argue that it has been frustrated from completing its contractual obligations.

Frustration is a legal principle outside of the contract which allows you to walk away from further performance. It does **not** give you the right to compensation for the loss of the remaining contract and may still leave you liable for issues connected with your performance up until the date of 'frustration'.

- Do you want to be released from the contract?
- Is contractual performance impossible – not difficult/expensive?

Frustration is **only** available where contractual performance is **impossible**¸ not simply difficult or expensive.

However, this cannot be used as an argument where:

a) the parties have contractually agreed the consequences of the event (for example by the use of a force majeure clause),

b) an alternative method of performance is possible

c) just because performance has become more expensive or (d) because a party has been let down by one of its suppliers.

It must have become physically or commercially impossible to fulfil the contract which is incredibly difficult to prove.

The following factors will be relevant for a court in deciding if this argument works:

a) terms of the contract

b) the factual background

c) knowledge of risk at the time of entering the contract

d) ability to foresee and factor the risk of COVID-19 into project delivery.

If this argument fails, you will most likely be in breach of contract.

9. JCT: Force Majeure

Clause 2.19.17 JCT DBSub/C 2016 “force majeure” as constituting a Relevant Event (presumably intentionally) without defining what “force majeure” actually includes.

Relevant Events entitle the contractor to an extension of time and may also equate to an event c.7 JCT DBSub 2016 entitling either party to terminate the contract – force majeure is not expressly included under the sub-contract (although it is in the corresponding main contract), but another ground may be relevant for the purposes of termination. Force majeure’ is not a Relevant Matter and therefore gives no entitlement for the contractor to loss and expense as a result of disruption caused by the ‘force majeure’ event (as with exceptionally adverse weather – which also allows the contractor extra time as a Relevant Event, but not extra money as it is not a Relevant Matter).

The downside to the lack of definition of “force majeure” is that the party seeking to rely on it must prove that works have experienced an unexpected and exceptional event that allows one party to terminate or claim under the contract without being liable for damages, i.e. an unexpected and disruptive event that may operate to excuse a party from its obligations under a contract.

10. NEC; Force Majeure

Under NEC3 Sub, c.60.1(19) – the equivalent to force majeure - allows the contractor to claim a compensation event where it:

a) stops the Contractor from completing the works OR stops the Contractor from completing the works by the date shown on the Accepted Program,

b) neither Party could prevent it and

c) an experienced Contractor would have judged it at the Contract Date to have such a small chance of occurring that it would have been unreasonable for him to have allowed for it.

Only if the above test is satisfied will the contractor allow the contractor to claim both time and money and give rise to an event of termination under NEC3 Sub c.91.7 where the delay lasts for more than 13 weeks with such significant consequences.

However, be careful as often these clauses are changed through bespoke amendments to remove your ability to claim money leaving you with just an extension of time.

11. Other

Many of the following self-analysis questions may relate to all or any of the above.

- Do clauses work the same in contracts above (with clients) and below (with suppliers)?
- Is there a risk register? Does it cover this risk? What does it say?
- Are you collating diary notes and other evidence to support your decisions and compliance with the contractual framework?
- Do you have a duty to mitigate, i.e. minimise the loss/delay/costs resulting from COVID19? What have you done about it? What is your evidence?
- What insurance is relevant – public liability if you are to continue contractual performance? Employer's liability to cover employees if you are continuing contractual performance? Business continuity insurance does not usually cover pandemics and epidemics, but does yours if you have it – it might do?

Building a claim is a forensic approach matching documentary evidence directly supporting each item of your claim to being directly caused by the events on which you are relying under clauses in your contract to give you contractual relief. Guestimates and unproven claims fail in nearly all cases and disputes. Doing the labour-intensive claims compilation work makes it easier for a judge/adjudicator/client to agree with you and harder for them to reject your position.

12. Mitigate the risk and get advice

As part of your business continuity plans, you should undertake an audit of your existing contracts to check the terms for protection.

On any new contract ensure you have the right to claim time and money where you experience disruption due to reasons beyond your reasonable control and ensure your duty to mitigate is only to the extent that you can take reasonable steps to do so.

Good legal drafting should provide clarity and resolution for any such issue and this should now include unknown viruses, or more particularly 'biological contamination'.

13. Contractual wisdom

ECA has produced other guidance notes downloadable from our website. These include Policy Procurement Notes issued by Government, Government's guidance on responsible contractual behaviour and the CLC's Guide to collaborative contractual behaviour.

Government **cannot** force its hundreds of procurement points to follow the same advice/non-legislative rules as to do so would be to undermine local democracy and behave in an anti-competitive way.

Also note, that some procurement authorities within Government may remain outside the definition of a 'contracting authority' for security, public interest and other reasons.

Those operating with public sector clients are advised to consult these guidance notes on the relevant PPNs and the PPNs themselves as they outline relaxation of the rules and flexible commercial arrangements to ensure continuity of public services during COVID19. Contractors can proactively draw these to their clients' attention and work with those clients

to ensure continuity of public services, and consequently their own workflows during COVID19

ECA is, by virtue of being the only engineering services sector body on the Construction Leadership Council COVID-19 taskforce, leading the CLC workstream on contractual behaviour, creating a pan-industry group of legal specialists who have worked hard to ensure the Government recognises the risk of wide-spread contractual disputes leading to insolvencies in our sector. The result is Government Cabinet Office Guidance and CLC Guidance – available on our website.

Both of which recognise that parties must leverage their contractual positions to preserve their legal positions, but strongly encouraging parties to simultaneously and proactively seek to establish a commercial dialogue with a view to reaching a binding commercial settlement amending the original contract recognising the impact of COVID-19 and accommodating it in a fair and proportionate way.

If you are in the process of negotiating a contract (especially if you are have already started works on site) you need to think very carefully about what commercial amendments you may need to agree to take into account what are likely to be significant delays and limitations on your productivity (i.e. method and sequence of working).

If the rule of thumb for negotiating is to '*only accept risk within your control and knowledge, or which you can quantify and price*', you will want to include specific wording that allocates the risk of Covid-19 and entitles you to time and/or money and to terminate in the event of force majeure – the definition of which should include pandemics.

You should also consider the secondary implications on any contractual obligations regarding management standards can do to maintain standards and processes and whether these are still viable – these may include obligations of site contamination and/or security.

Check your contracts up and down stream within the supply chain to make sure you are able to manage your liability and exposure in both directions and that you are not put at risk.

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